The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

October 13, 2017

As of 10/13/2017		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	22,871.72	98.05	0.43	2.24	15.73	26.37
S&P 500	2,553.17	3.84	0.15	1.95	14.02	19.70
NASDAQ 100	6,092.45	27.88	0.46	1.09	25.27	26.84
S&P MidCap 400	1,818.82	0.39	0.02	1.56	9.53	19.69
Russell 2000	1,502.66	-7.56	-0.50	1.32	10.71	23.59

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	1.49	Euro/Dollar	1.18	0.75
5-Year	1.90	Dollar/Yen	111.85	-0.72
10-Year	2.27	Sterling/Dollar	1.33	1.68
30-Year	2.81	Dollar/Cad	1.25	-0.47

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

On October 1st, Catalonia, the semiautonomous and prosperous region of Spain, conducted a referendum to determine whether or not to secede from Spain. Catalonia has its own unique language and culture, and it has Spain's highest concentration of businesses and middle-class professionals. Catalans have long complained that they are unfairly used as a source of taxes to fund other less affluent regions of the country. Because the Spanish government in Madrid declared the referendum illegal and many disagreed with the idea of a referendum, 57% of the Catalans chose not to even vote. Of the 43% that did vote, about 90% voted for independence. This past Tuesday night, the Catalan president, Carles Puigdemont, declared independence but immediately suspended the declaration pending negotiation talks with Madrid. Spain's president, Mariano Rajoy, trying to clarify the ambiguity of Puigdemont's announcement, has given Catalonia a deadline of this Monday (10/16) at 4:00 am EST to confirm whether or not it is actually declaring its independence. If Puigdemont says "yes," Spain will give Catalonia until this Thursday (10/19) at 4:00 am EST to retract its decision or it will trigger Article 155 of its constitution which allows Madrid to dissolve the Catalan government and declare snap elections for a replacement government. A resolute declaration of independence on the part of Catalonia will negatively impact Spanish financial markets.

Economy

The most anticipated report this week was the retail sales report, which was released on Friday. Retail sales increased 1.6% in September and are now up 4.4% year-over-year. The all important control category, which excludes food service, autos, gas and building materials, advanced by 0.4%. The best performing sectors were motor vehicles and parts (+3.6%) and gas stations (+5.8%). It now appears that real consumption growth will increase close to 2.5% in the third quarter. Earlier in the week, the JOLTS report (job openings and labor turnover survey) showed 6.1 million job openings in August. The "quits" rate was unchanged at 2.1%, and the layoffs and discharges rate were little changed at 2.1% and 1.2%, respectively. Overall, when reviewing the last 12 months, the net employment gain amounts to 2.1 million. On Thursday, the producer price index showed an increase of 0.4% in September matching expectations. Producer prices are now up 2.6% year-over-year. Finally, on Friday, the September consumer price index displayed an advance of 0.5%, which was slightly below expectations. The core CPI (excludes food and energy) increased only 0.127%.

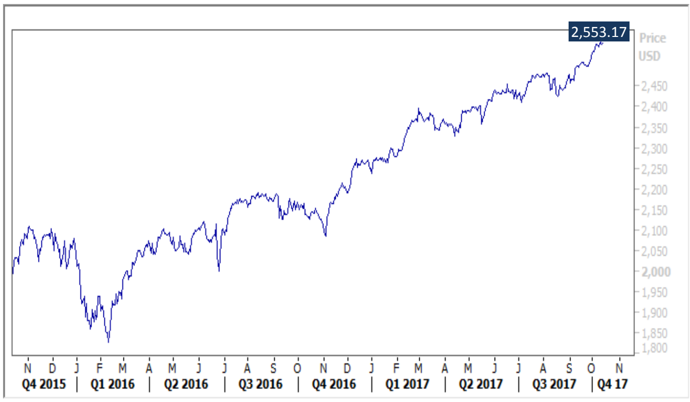
Fixed Income/Credit Market

With the Volatility Index (VIX) trading at 9.6, approximately 10 points below its lifetime average, investors continue piling money into high yield assets. According to Bloomberg, high yield retail funds reported an inflow of $967MM for the week ended October 11, the most in 12 weeks. The global demand for yield has driven asset prices higher, while pushing credit spreads to multi-year lows. The 5-year BB and B-rated composites are trading 73 basis points (bps) and 81 bps below their 5-year averages, respectively. Investment grade bond spreads are also at multi-year lows. The 5-year AA, A and BBB-rated composites are currently 13 bps, 17 bps, and 34 bps below their 5-year averages, respectively. It is hard to predict when credit spreads will reverse course and begin to widen, but with the high yield corporate default rate hovering around 1% according to JP Morgan, credit stress appears very low at the moment.

Equities

Equity market activity was muted this week due to in line economic reports and limited third quarter company reporting. The earnings reports were mainly centered on the money center banks, which showed satisfactory results, yet certain business lines such as trading were relatively weak. Accordingly, the financial sector declined during the week. Another sector of weakness was telecommunications due to news of a reduction in video subscribers. Finally, the healthcare sector witnessed some decline due to the Trump administration signing an executive order that would end cost-sharing subsidies to the health insurers under the Affordable Care Act. The above-mentioned sector weakness was offset by strength in utilities and consumer staples, which benefited from a market rotation into income assets. An area of notable strength was the international markets, which are benefiting from continued foreign central banking stimulus while the U.S. central bank is in the process of tightening.

S&P 500



Our View

Rising equity values and the absence of volatility has been a consistent theme this year even with the U.S. Fed slowly increasing interest rates and beginning the process of gradually decreasing the size of its balance sheet. The previously mentioned statement should come as no surprise given the enormous amount of liquidity that has been pumped into the U.S. economy since the financial crisis. Moreover, according the Federal Reserve, the aggregate amount of reserves above the penalty-free band at depository institutions stood at over $2.16 trillion at the end of September. This is roughly $500 billion less than the peak achieved in August of 2014, but still incredibly high. Ample liquidity has made it inexpensive for consumers, corporations and the public sector to increase or refinance their debt loads. Using the U.S. commercial paper spread to T-bills as a proxy for liquidity availability, the current spread of 24 basis points (bps) is 18 bps below the average going back to 1996. By comparison, the aforementioned spread increased to over 300 bps in September of 2008. Moving forward, we believe the Fed will continue to gradually remove excess liquidity from the economy as long as inflations stays within close proximity to their 2% target.

COMING UP NEXT WEEK		**Est.**
10/16 NY Fed Manufacturing	(Oct)	20.70
10/17 Industrial Production MM	(Sep)	0.3%
10/17 Capacity Utilization MM	(Sep)	76.2%
10/18 Housing Starts Number MM	(Sep)	1.180M
10/19 Philly Fed Business Index	(Oct)	22.0

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